

# State and Local Government Fiscal Position, 1981

**T**HE State and local government surplus on a national income and product accounting (NIPA) basis was \$36.5 billion in 1981, up \$7.5 billion from the 1980 surplus. The increase in the surplus reflected a larger increase in receipts than in expenditures, although both showed a slower rate of growth than in the previous year. Of the \$7.5 billion increase, \$5 billion was in the surplus of social insurance funds and a \$2.5 billion increase in the surplus of all other funds. The increase in the surplus of all other funds was the first since 1977.

## Receipts

State and local government receipts increased 8½ percent in 1981, compared with 10 percent in 1980 (table 1). The deceleration was the result of a decline in grants-in-aid; general own-source receipts accelerated, increasing 11 percent, compared with 9 percent in the previous year. Personal taxes and nontax receipts did not contribute to the acceleration in general own-source receipts, as income tax and nontax receipts growth slowed somewhat. Income tax growth was limited by the use of indexation in eight States. (For a discussion of indexation, see the February 1981 SURVEY OF CURRENT BUSINESS). Corporate profits tax accruals did contribute to the acceleration; they declined 5 percent, compared with 6½ percent in 1980. Sales and property taxes both registered rapidly accelerating growth. Sales tax growth, which had been held down by legislated reductions in 1979 and 1980, was strengthened in 1981 by legislated increases of \$1.0 billion. More than one-half of this increase was in motor fuel taxes; 26 States increased excise taxes on gasoline. These taxes, which are unchanged from 1980, would have declined about \$0.6 billion in the ab-

sence of these legislative actions. In addition, a number of States now have ad valorem gasoline taxes; therefore, as gasoline prices increased, the tax increased as well. Increases in general sales taxes (chiefly in Minnesota, Nevada, Ohio, Washington, and West Virginia) added another \$0.2 billion to sales taxes; legislative actions added to receipts for the first time since 1977. Sales taxes in the Chicago and New York City metropolitan areas were increased, and the increases were dedicated to funding of transit operations.

Indirect business property taxes increased more rapidly than in any year since 1977. A 7½-percent increase occurred despite legislative actions to hold down growth in several States. The largest of these was in Massachusetts, where voters imposed a reduction of approximately \$0.5 billion (at annual rates) on property taxes and also limited future growth. However, in the Nation as a whole, it appears that the decline over the previous decade in average effective property tax rates ended in 1981.

The rate of increase in other indirect business taxes was slower than in 1980 but still more rapid than any other revenue category shown in table 1. The rapid growth of the past several years represented, for the most part, energy-related taxes and charges.

Federal grants-in-aid declined about \$1 billion in 1981, slightly more than 1 percent, compared with a 10-percent increase in 1980. Major declines occurred in general revenue sharing (34 percent)—the State government share ended in 1980—and in the employment titles of the Comprehensive Employment and Training Act (CETA), which were terminated by the end of 1981. Highway and water treatment capital grants also declined in 1981, but they were partly offset by a sizable increase in grants for mass transit construction. The only other category to increase significantly (about 13 percent) was public assistance. All other grants-in-aid taken together increased 1 percent.

Contributions for social insurance increased 15½ percent, much more

Table 1.—State and Local Government Receipts, NIPA Basis

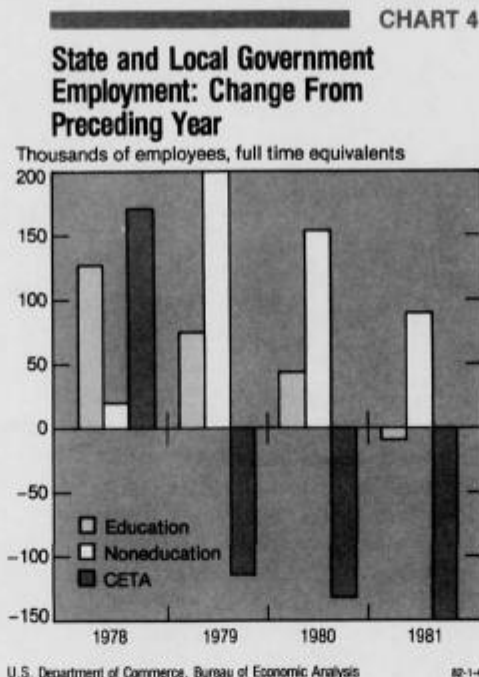
	Calendar years								
	Billions of dollars					Percent change			
	1977	1978	1979	1980	1981	1978	1979	1980	1981
Receipts.....	298.6	327.1	351.2	381.8	416.8	9.8	7.3	9.1	8.8
General own-source receipts.....	268.4	295.8	328.8	354.5	393.4	8.2	7.8	8.0	10.9
Personal tax and nontax receipts.....	58.4	62.9	70.8	80.7	91.9	13.3	10.4	14.2	13.0
Income taxes.....	30.9	35.5	38.8	44.9	51.9	15.1	9.2	16.9	15.4
Nontaxes.....	18.9	21.4	24.5	27.9	31.4	13.2	14.4	12.8	12.8
Other.....	0.7	7.0	7.5	7.9	8.7	5.2	6.0	7.0	10.3
Corporate profits tax accruals.....	11.0	11.7	13.0	12.2	11.6	6.7	11.9	-6.6	-5.1
Indirect business tax and nontax accruals.....	141.0	149.0	153.0	171.6	189.0	6.3	6.0	7.9	10.6
Sales taxes.....	64.1	71.8	76.9	82.9	92.7	10.8	8.3	7.7	11.8
Property taxes.....	63.4	63.3	64.4	67.5	72.6	.8	.7	4.9	7.5
Other.....	13.5	15.0	17.7	21.2	24.6	10.8	17.9	20.2	15.9
Contributions for social insurance.....	22.1	24.5	29.1	31.5	36.4	11.3	14.5	11.9	15.7
Federal grants-in-aid.....	87.5	77.3	80.4	88.6	87.8	14.4	4.1	9.5	-1.2
Addenda: Receipts, excluding selected law changes:									
Total.....	397.4	329.5	358.2	391.3	424.7	10.8	8.8	9.4	8.4
General own-source receipts.....	297.8	327.7	349.7	372.4	401.3	8.0	9.7	9.1	10.6

than in 1980 but only modestly more than in 1979. The deceleration in 1980 was accounted for by a \$0.4 billion refund under the cash sickness (temporary disability insurance) program administered by the State of California. Because there was no similar refund during 1981, the accelerated growth represented mainly a return to normal conditions.

### Expenditures

In 1981 expenditures registered the smallest increase in 20 years—only 7 percent (table 2). The deceleration from a 9½-percent increase in 1980 was concentrated in the purchase of structures, which fell 4.5 percent after a 12-percent increase in 1980, and in the direct relief component of transfer payments, which increased only 5½ percent after a 14-percent increase.

Total purchases increased 7½ percent, compared with 10 percent in 1980. Compensation increased at about the same rate as in 1980. Real compensation was unchanged in 1981, but the lack of change masked shifts in types of employment. State and local government employment financed through CETA declined in 1981 for the third consecutive year (chart 4). In 1978, CETA hiring had been largely in addition to normal hiring by States and localities. Given the very small 1978 increase in employment other than in education, it appears that much of the CETA hiring was in lieu of normal hiring. In 1979, the decline in CETA hiring was



more than matched by increases in normal hiring, so that total employment increased about 1½ percent. In 1980 and 1981, the continued declines in CETA employment were not balanced or offset by strong normal employment growth; in fact total employment actually declined slightly in 1981. (The 1981 decline in education employment appears to have occurred at the State level, reflecting declines in enrollment in public institutions of higher education.) It seems likely that better qualified CETA employees, because they were more easily absorbed into the permanent workforce, were "skimmed" off in 1979 as managers

anticipated continued declines in CETA funds (the public employment titles of CETA were terminated toward the end of 1981). In 1980 and 1981, many governments had run down surpluses accumulated in 1978 and earlier, so that they could no longer fund both normal hirings and the absorption of former CETA employees.

The decline in the purchase of structures was concentrated in two areas: education and sewerage. A \$1 billion decline in construction for education was caused, at least in part, by the termination of the State government share of general revenue sharing. In the latter half of the 1970's, much of this grant funding supported construction of elementary and secondary schools. A \$1 billion decline in sewer and treatment plant construction probably is related to uncertainty about continued Federal funding from grants-in-aid under the Clean Water Act. Spending for other types of structures showed little change from 1980.

Transfer payments to persons increased 8 percent, compared with 11 percent in 1980. As noted above, the deceleration occurred in the direct relief transfers, which increased only 5½ percent, compared with 14 percent in 1980. This deceleration had two probable causes: (1) in the first half of 1981, the modest improvement in the economy probably held down the growth of the welfare caseload; (2) in the second half of the year, tighter administrative controls, at least partly in anticipation of Federal efforts to reduce welfare outlays, caused a decline in these transfers. Further growth reductions in several States were due to decisions to reduce or eliminate cost-of-living adjustments in payments under the Aid to Families with Dependent Children programs.

Interest received by governments, which in the NIPA's is netted against interest paid, continued to outpace all major categories of expenditures, thus slowing total expenditures growth. Dividends received by social insurance funds, which are also netted against expenditures in the NIPA's, increased 13.5 percent, compared with 4½ percent in 1980. This acceleration reflected the decision of fund managers to shift investments toward equity holdings after several years of concentration on interest-bearing investments.

Table 2.—State and Local Government Expenditures, NIPA Basis

	Calendar years								
	Billions of dollars					Percent change			
	1977	1978	1979	1980	1981	1978	1979	1980	1981
<b>Expenditures.....</b>	<b>270.0</b>	<b>298.4</b>	<b>324.4</b>	<b>355.0</b>	<b>380.3</b>	<b>10.9</b>	<b>8.7</b>	<b>9.4</b>	<b>7.1</b>
Purchases of goods and services.....	250.6	279.2	305.9	335.8	361.1	11.4	9.6	9.8	7.5
Compensation of employees.....	144.0	157.5	172.3	187.4	203.3	9.3	9.4	8.7	8.5
Structures.....	31.0	37.5	40.3	45.3	43.2	21.0	7.4	12.4	-4.5
Medical vendor payments.....	15.7	17.1	19.4	21.5	24.2	9.4	13.2	10.8	12.7
Other purchases.....	59.9	67.1	73.9	81.7	90.3	12.1	10.1	10.5	10.5
Transfer payments to persons.....	29.7	32.8	35.0	38.9	42.0	10.3	6.8	11.0	8.1
Benefits from social insurance funds.....	12.5	14.1	15.9	17.6	19.4	13.3	12.3	10.8	10.3
Direct relief.....	13.4	13.6	14.1	16.0	16.9	1.2	3.3	13.8	5.4
Other.....	3.8	5.1	5.1	5.3	5.7	32.3	.8	3.8	8.7
Net interest paid.....	-4.0	-6.2	-8.8	-10.8	-12.8				
Interest paid.....	13.7	14.9	16.3	17.6	19.4	8.9	9.5	7.8	10.5
Less: Interest received by government.....	17.7	21.1	25.1	28.4	32.3	19.2	19.0	13.3	13.5
Less: Dividends received.....	1.2	1.5	1.5	1.6	1.8	21.7	1.8	4.5	14.0
Subsidies less current surplus of government enterprises.....	-5.1	-5.7	-6.3	-7.4	-8.2				
Subsidies.....	.2	.2	.3	.4	.4	13.8	36.8	8.3	13.6
Less: Current surplus of government enterprises.....	5.4	6.0	6.7	7.7	8.6	11.7	11.7	15.5	10.9
Less: Wage accruals less disbursements.....	0	.2	-.1	0	0				

*Fiscal position*

The State and local government sector, excluding the operations of social insurance funds, registered a surplus of about \$4.5 billion in 1981, up from \$2 billion in 1980. The increase in the other funds measure—the first since 1977—occurred despite the decline in Federal grants-in-aid. A number of factors appear to have contributed: (1) expenditures growth slowed in 1981 in anticipation of Federal cutbacks larger than those that actually occurred; (2) welfare-related spending increased less rapidly than did Federal grants for public assistance, indicating some measure of success in State and local efforts to shift the burden of such spending toward the Federal Government; (3) legislative actions increased tax receipts, especially in such States as Minnesota and Ohio where previously accumulated balances had been run down; and (4) many local governments apparently were willing to allow property taxes to increase more rapidly than in recent years. Further, over the past several years strong revenue growth has occurred in certain mineral-wealthy States. Such growth continued, although probably less rapidly, in 1981, so while some of these States (Texas and Louisiana) continued to accumulate surpluses, many other States and localities continued to move toward or into deficit.

This other-funds measure has usually registered a deficit; prior to 1972, when general revenue sharing funds accounted for much of the surplus, the last surplus was recorded in 1947. Because capital spending by government is combined with current spending in the summary NIPA presentations and because much of the capital spending by States and localities is funded by long-term borrowing, the "normal" fiscal position of the other-funds measure has been a deficit.<sup>1</sup>

1. This and other characteristics of the surplus and deficit in the NIPA framework are discussed more fully in "State and Local Government Fiscal Position in 1978," in the December 1978 issue of the *Survey of Current Business*.

(Billions of dollars)

	1978	1979	1980	1981
NIPA surplus or deficit (-)				
Total	29.6	25.7	29.1	35.5
Social insurance funds	28.0	23.9	26.9	32.1
Other funds	9.0	2.9	2.1	4.4

*Outlook*

In 1982, total receipts are likely to increase somewhat more slowly than in 1981, about 8 percent. This increase is predicated on acceleration of general own-source receipts to about a 12-percent increase. A part of this acceleration will reflect the first full-year effects of legislative increases effective after the middle of 1981, primarily in sales taxes. It also assumes acceleration in personal income taxes as a result of actions in certain states limiting the tax-reduction effects of indexation. Minnesota and California have already acted in this direction, and others are likely to do so in 1982 legislative sessions. Further, this acceleration is predicated on larger increases in property taxes stemming from maintenance of average tax rates and inflation-generated increases in assessments, as well as from additions to the stock of taxable real property.

Several States and localities have run down general fund balances to a point where major expenditures reductions, tax increases, or both will be necessary. Minnesota, Ohio, and Washington have enacted sizable tax increases, and a sales tax increase is likely in Massachusetts. New York and Chicago transit districts are receiving enhanced support from new and increased taxes, although a portion of the Chicago tax package has been invalidated by the courts. In some other States the 1982 spring legislative sessions will be dominated by tax issues.

In California, tax increases or major spending reductions appear inevitable. The State began fiscal year 1979—the first year of Proposition 13—with a surplus of about \$4 billion. It began fiscal 1982 with a surplus of \$0.7 billion. Outlays thus exceeded current receipts by an average of about \$1.0 billion annually for the last 3 fiscal years. As of the end of calendar year 1981, the remaining general fund surplus had been used, and short-term borrowings from highway and other special funds had been made.

Federal grants-in-aid will decline further in 1982, probably more than 5 percent. Grants for transit construction, which actually increased in 1981, are likely to decline; grants for entitlement programs, such as Medicaid, are slated for cutbacks.

Expenditures increases will remain well under 10 percent. Termination of CETA employment at the end of 1981 will provide a negative effect on the 1982 change in employment. Overall, compensation increases will likely be limited to growth in average pay—perhaps 7 to 8 percent. Construction outlays are unlikely to increase significantly; long-term borrowing for public capital purposes was level in 1981, grants-in-aid for such purposes will be cut further in 1982, and current revenue will be preempted for current operations spending in most governments. Increases in other purchases from businesses will probably no more than match increases in costs.

The 1982 surplus on the NIPA basis will probably reach \$41 billion, of which about \$88 billion is the social insurance fund surplus, and \$3 billion is the surplus in other funds. If property values fail to increase sufficiently to support projected property tax growth, or if legislatures decide against proposed tax increases, then the other funds measure could well move into deficit.